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Chairman Marc Spitzer
Commissioner William A. Mundell
Commissioner Mike Gleason
Commissioner Jeff Hatch-Miller

Re: Efforts that should be undertaken by the Corporation Commission to help reduce the price of gasoline in Arizona.

Dear Colleagues:

Gasoline prices have hit record highs, and some experts are predicting that prices could climb as high as $3 per gallon by summer's end. These increases are placing pressure on the pocketbooks of individual consumers and threaten to damage our state's economy. I believe it is incumbent on each statewide official to use every weapon in their arsenal to try to bring relief at the pumps this year. While the Corporation Commission has not traditionally regulated the price of gasoline,[1] there are steps we can take to provide Arizonans with information about these energy cost increases and to help bring down gasoline costs over time.

The ACC should urge Kinder Morgan to consider further expansion of its eastern pipeline and request that FERC examine and possibly alter the tariffs on Kinder Morgan's eastern line to incentivize expansion.

If Arizona is to reduce the price of gasoline, we must work to increase supply lines into the state. In particular, we must do what we can to encourage the speedy expansion of the Kinder Morgan eastern pipeline that runs from El Paso and connects with the Tucson tank farm. To its credit, Kinder Morgan has initiated the process of expanding the eastern line, choosing to "loop" the current 12" line with larger 16" segments, and the 8" line with larger 12" segments. I believe Kinder Morgan should also consider expanding the eastern line by looping with 20" segments. If looping with larger pipe would unduly delay construction, I would urge Kinder Morgan to consider construction of a second pipeline from the east, in addition to its looping project. To initiate this discussion, I have asked to meet with Tom Bannigan, Kinder Morgan's President of Products Pipelines.

[1] Article 15, Section 3 of the Arizona Constitution confers upon the Corporation Commission broad regulatory authority over public service corporations which "furnish gas, oil, or electricity for light, fuel or power." The question of what the state's Founding Fathers meant by oil for fuel has never been litigated and the Commission to date has not chosen to regulate oil and gasoline.

Moreover, in order to encourage further expansion of the eastern line, it may be necessary for the Federal Energy Regulatory Commission (FERC) to consider altering its tariffs on the line. The current western line tariff is considerably higher than the east line, serving as a disincentive for Kinder Morgan to expand the eastern pipeline.[2] FERC should investigate changing these tariffs in such a way that Kinder Morgan would be more likely to expand the eastern line to at least match the size of the 20'' line from the west, which in turn would increase supplies of gasoline in Arizona. This potentially would have the result of lowering prices at the pump. Furthermore, FERC should bring to bear any other tools it might have available to spur the expansion of this critical gasoline line in Arizona.

Accordingly, I have written a letter to FERC requesting that they commence an examination of these tariffs and how they might be reconfigured and of any other methods that could be utilized to encourage expansion of the El Paso to Tucson pipeline, or the construction of another gasoline pipeline into the state.

The ACC should encourage the building of an Arizona refinery

ACC Commissioners, as well as other Arizona officials, should do everything possible to encourage the building of a new refinery in Arizona. Although a refinery has not been built in the United States in more than two decades, there is clear momentum for a refinery in Yuma County, where public officials, local businesses and many residents have banded together to support a project proposed by Arizona Clean Fuels. It is estimated that this refinery could pump as much as 150,000 barrels of gasoline, jet fuels and diesel per day into our state's overall fuel supply.

The need for a new refinery is evident. Today, demand for gasoline far exceeds what is produced in the Southwest. There are currently 13 refineries in California that produce approximately 46.2 million gallons of gasoline a day. This amount is not adequate to cover the demand of California, Nevada, and Arizona, which in turn forces the refineries to import about 4.2 million gallons a day. In essence, the refining capacity in the Southwest is maximized and a new refinery is necessary to relieve the pressure.[3]

I urge the Governor and the director of the Department of Environmental Quality to move forward with the permitting process for this project as expeditiously as possible, while not sacrificing the rigorous environmental review under way. It is estimated that if ground can be broken this year on a new refinery, it could be producing gasoline for Arizona markets by the year 2008. While this clearly won't provide relief this summer, we must begin planning for the state's inevitable growth and attendant gasoline needs. To that end, I have drafted a letter to ADEQ Director Steve Owens regarding this matter and I invite each of you to sign on.

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[2] Kinder Morgan charges 75.18 cents per barrel on gasoline that travels on its El Paso to Phoenix route and 55.85 cents per barrel from El Paso to Tucson. In contrast, KM charges 132.72 cents per barrel for gasoline traveling from Watson, CA to Phoenix and 162.28 cents from Watson, CA to Tucson.

[3] The data in this paragraph is taken from the following: Elizabeth Douglass, <u>Upward Pressure at the Pump</u>, Los Angeles Times, July 8, 2003.

Once this project receives the green light from ADEQ, I believe the Commission's pipeline safety staff should prepare to provide guidance on any potential pipeline safety issues associated with the building of new gasoline or crude oil pipelines to or from the new refinery.

Commissioners should hold one-on-one meetings with executives from gasoline companies with business in Arizona

National oil executives owe Arizonans a clear and cogent explanation of their current business practices in our state, including what they are doing to help bring down the high cost of gasoline here, as well as a defense of their skyrocketing profits. A survey by the *Arizona Republic* found that the combined profits of the top five gasoline suppliers in Arizona – Valero Energy, ChevronTexaco, ConocoPhillips, BP plc, and ExxonMobil – climbed 99 percent from 2002 to 2003. Some companies reported even more dramatic gains, including one that recorded a 539 percent increase in profits.[4]

If oil executives believe price gouging is not involved, they should state what they do believe is driving these profits and price increases in the Southwest. For instance, are the higher gasoline costs in Arizona primarily due to inadequate refining capacity, the lack of pipeline delivery capacity, marketing costs, state fuel blend requirements, taxes on gasoline or consolidation of refineries in the West and nationally? Knowing this will allow state and federal lawmakers and regulators to better home in on solutions. Recently, several oil executives participated in conference calls with reporters to answer questions about gas prices. They should do the same or more with state officials.

The Corporation Commission is in a position to convene these meetings with oil executives, as we already possess regulatory oversight over other aspects of their business. Toward this end, I will be asking oil executives that sell gasoline in our state to voluntarily meet with me and any other Commissioner who indicates an interest.

Sincerely,

Kris Mayes
Commissioner

Cc: Gov. Janet Napolitano
Senate President Ken Bennett
House Speaker Jake Flake
Ernest Johnson
Brian McNeil

[4] Max Jarman, Suppliers Reap Gasoline Profits, Arizona Republic, 4/25/04.